REGIONAL DEVELOPMENTS

Pacific Basin*

I. Australia

A. Design Infringement Case: Prelitigation Strategy Implications

J. Rapee & Co. Pty. Ltd. v. Kas Cushions Pty. Ltd. & Anor,[1] a decision of the federal court handed down on October 9, 1989, is particularly relevant to the preparation of prelitigation contracts with respect to patents, trademarks, designs, and any other contract that seeks to impose a "no-challenge" restriction of the kind that was held invalid in *Lear v Adkins.*[2]

The applicant was the registered proprietor of two designs for chair pads and cushions registered pursuant to the Designs Act 1906. The features of both designs included piping around the perimeter with rounded rather than angled corners, ties to secure the pads to the chair, and circulator stitching at "tufting" points. The applicant manufactured and imported chair pads and cushions for resale to major department stores and retailers. Although at the date of the commencement of the proceedings the applicant had not yet manufactured or imported items bearing the second design, it intended to do so. The respondents manufactured and imported chair pads and distributed them throughout Australia.

Sometime in March 1987 the first respondent agreed with the applicant not to import or otherwise deal in chair pads that came within the scope of the first design registration. The applicant alleged that the respondent breached this agreement and infringed its monopoly in both its designs by selling a fraudulent imitation of the designs. The respondents cross-claimed, seeking expungement of the designs from the Register, alleging that the applicant's designs: (i) were

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1. 15 I.P.R. 577 (1989).
2. 395 U.S. 653 (1969).

comprised of a method or principle of construction; (ii) were not novel as they were in the public domain before the priority date; (iii) differed only in immaterial features or features commonly used in the trade; and (iv) were an obvious adaptation of a design that was published or used before the priority date in respect of another article.

At the hearing evidence was given by numerous trade witnesses and representatives of the respondents. The respondents sought to establish that the features of the design registrations, namely the piping around the perimeter, the circulator stitched tufting, and rounded corners, had been incorporated in similar chair pads in various degrees before the priority date of the first design registration. However, no identical articles said to constitute prior use were produced. Various advertisements and promotional materials were also tendered and admitted into evidence by the respondents to try and prove prior publication of the design before the priority date.

B. Decision

The federal court dismissed the applicant's claim and upheld the cross-claim for expungement. Judge Gummow found insufficient publication, as the material in the catalogues had not been adequately disclosed to the public or made available for inspection by the public. The evidence of the trade witnesses did not establish prior publication or prior use, but Judge Gummow did find that it was relevant in determining the novelty aspect of the designs.

A design will not be held invalid for registration merely because it comprises a number of features that are similar to earlier designs if there are other differing elements. Judge Gummow held, however, that, before priority date, the features of the designs were well-known and commonly used by those in the trade of manufacturing chair pads. The two designs were combinations of common trade variants, and therefore their registration was invalid; accordingly, expungement of the registration from the Register was ordered.

Although the applicant did not submit that the March 1987 agreement operated to bar the first respondent from seeking cancellation of the designs, Judge Gummow observed that an agreement attempting to restrain a challenge to a design monopoly might offend public policy. On the present facts, however, he held that even if the agreement was valid, there had been no breach, as the respondents' goods were not fraudulent or obvious imitations of the applicant's designs.

C. Comment

Many intellectual property conflicts are settled before or during litigation. It is also not unusual for a registered proprietor to extract an agreement from, for example, a licensee, not to challenge the proprietor's registration in the future. Judge Gummow, however, sees such agreements as offending public policy and refers to two U.S. cases to support this proposition: *Lear v. Adkins*[3] and *Troxel Manufacturing Co. v. Schwinn Bicycle Co.*[4] Although the comment is obiter dictum, it is in line with the principles in a growing number of jurisdictions.

II. Hong Kong

A. Taxation of Trading Profits: The *Exxon* Case

Until recently it had been thought that Hong Kong re-invoicing operations did not give rise to any Hong Kong profits tax liability where the operations were limited to "paper-pushing" in relation to the taxpayer's offshore activities.

In the recent case of *Exxon Chemical International Supply SA v. Commissioner of Inland Revenue*[5] tax was imposed on Exxon Chemical, a Hong Kong company that bought petroleum products from affiliated companies outside Hong Kong and resold them to other affiliated companies outside Hong Kong. Upon receiving a purchase order from an overseas affiliate, Exxon Chemical's Hong Kong office would transmit the order to a U.S. affiliate, which would identify a source of supply, purchase the goods on behalf of Exxon Chemical and arrange for direct shipment to the buyer. The U.S. affiliate received a fee from Exxon Chemical for these services.

1. *General Principles*

Hong Kong profits tax (currently at 16.5 percent) applies only if business is carried on in Hong Kong, and such business produces profits having their source in Hong Kong. The general test for source of profits is an "operations test," which looks to the location of the operations from which, in substance, the profits arise.

2. *Exxon's Argument*

Exxon Chemical conceded that it was carrying on business in Hong Kong by accepting orders and placing orders from its Hong Kong office, but argued that its profits had their source outside Hong Kong. Virtually all operations relating to the performance of the contracts of sale took place outside Hong Kong; therefore, Exxon argued, the profits should be treated as arising from offshore operations.

3. *The Decision*

Judge Godfrey of the High Court held that Exxon Chemical's profits had their source in Hong Kong and were therefore subject to Hong Kong profits tax. In his

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3. *Id.*
4. 465 F.2d 1253 (1972).
5. [1989] 1 H.K.R.C. 90-019, Hong Kong.

view Exxon Chemical's profits arose from a sales mark-up. That mark-up was effected by Exxon Chemical accepting purchase orders and placing corresponding orders with suppliers at a lower price. Both of these activities took place in Hong Kong. The activities of Exxon Chemical's U.S. affiliate and other contractors were not viewed as giving rise to Exxon Chemical's profits. Rather, the offshore activities were seen to give rise only to the profits earned by the contractors from their fees.

4. *Commentary*

The court was apparently influenced by an often-overlooked statutory provision, section 2 of the Hong Kong Inland Revenue Ordinance, which states that profits "from business transacted in Hong Kong" have their source in Hong Kong for tax purposes. Given that the sales contracts producing all of Exxon Chemical's income were entered into in Hong Kong, the court had no difficulty in concluding that all of Exxon Chemical's business was transacted in Hong Kong, and that its business profits therefore had their source in Hong Kong.

In similar situations in the past the generally accepted view was that a re-invoicer's profits arose from offshore operations of affiliates. Implicit in this view was the reasoning that trading profits did not arise from the mere signing of contracts. Rather, the buyer paid for goods that were delivered on time in marketable condition pursuant to the contract. Therefore, the activities involved in performing the sales contracts (obtaining the goods, inspecting them, shipping them, and so forth) were at least as important in producing trading profits as was the signing of the contracts. Where nothing occurred in Hong Kong but the formal conclusion of the contract, the "operations test" would deem the source of the sales profit as outside Hong Kong.

In rejecting this analysis, the court appeared to place special importance on the place of contracting. However, the court's view might well have been different if the performance-related operations had been conducted by employees of Exxon Chemical outside Hong Kong, rather than by affiliates who derived profits that were independent of Exxon Chemical's profits.

The Exxon case is currently on appeal. Meanwhile, several other cases involving the source of profits are pending at various levels of the Hong Kong judicial system. The volume of litigation on this issue reflects the current focus of the Hong Kong tax authorities on profits from international activities. In these circumstances careful planning in international operations involving Hong Kong is essential.

B. Exemption Clauses to be Restricted

Previously Hong Kong has had few restrictions on the use of clauses exempting liabilities. The recent enactment of the Control of Exemption Clauses Ordinance (the Ordinance), which is modelled on the United Kingdom's Unfair

Contract Terms Act 1977, will impose new restrictions in this area covering exemption clauses excluding or restricting liability in both contract and tort. Some exemption clauses are declared ineffective per se; others are subject to a test of reasonableness.

Where death or personal injury is caused by negligence, a person now cannot exclude any liability by any contractual term or notice. For other loss or damage caused by negligence, liability can be restricted if the restriction satisfies the requirement of reasonableness, guidelines for which are set out in the Ordinance. The existence of any term or notice exempting liability for negligence cannot of itself give rise to the defense of voluntary assumption of risk.

In consumer sales liability for breach of the seller's implied undertakings as to title of products or the conformity of goods with any description or sample, or as to their quality or fitness for a particular purpose, cannot be excluded by contractual terms. In nonconsumer sales liability for breach of such implied terms can be excluded only if it satisfies the requirement of reasonableness.

If one party is dealing as a consumer, or if the contract is in written standard terms of business, liability for breach or nonperformance of contract or alteration in the mode of performance cannot be excluded unless the exclusion is reasonable.

1. *Reasonableness*

Factors that are to be considered in deciding whether an exemption clause is reasonable under circumstances include: (i) the strength of the bargaining positions of the parties relative to each other; (ii) whether the customer received an inducement to agree to the exemption clause; and (iii) whether the goods were made to the special order of the customer.

The language in which the clause or notice is expressed is relevant in determining reasonableness. The consideration here is whether the language is a language understood by the party against whom the exemption clause or notice is pleaded. In Hong Kong there are people who are literate in Chinese, but not in English, and vice versa. All exemption clauses and notices should in the future be expressed in both languages.

2. *Conclusion*

Trading companies dealing with customers in Hong Kong on standard terms and conditions should review their exemption clauses in light of the Ordinance. In addition, any exemption clause included in a contract governed by Hong Kong law should be carefully drafted so as to be effective. In this respect it should be noted that the Ordinance has effect, notwithstanding that the contract is expressly stated to be governed by the law of some other country, if the choice of law appears to have been made mainly for the purpose of enabling a party to evade the operation of the Ordinance or if the other party is a consumer resident in

Hong Kong. It should also be noted that the Ordinance does not apply to international supply contracts.

III. Indonesia

A. New Patent Law

On November 1, 1989, the Indonesian Parliament passed a new Law No. 6/1989 on Patents. The previous ministerial regulations on patent application registrations dating back to 1953 were simultaneously withdrawn. The new Patent Law will come into effect on August 1, 1991. In the interim the entire process of registration has been frozen pending the training of patent examiners. During this period the government will prepare and issue detailed implementing regulations.

From 1953 until the passage of the Patent Law, the Patent Office had received over 13,000 applications for patent registrations. The vast majority of these were applications from foreigners. None of these applications had been granted in the absence of a patent law, and only those applications filed within ten years of the effective date (that is, since August 1, 1981) will be given the opportunity to re-register under the new provisions.

1. *Scope of Patent Coverage*

The new Patent Law defines the scope of patent protection as follows:

(i) A patent is a special right granted by the state to an inventor for a certain period so as to implement an invention in the field of technology.

(ii) A patent may be granted for new inventions that involve an inventive aspect (that is, not obvious to a person possessing ordinary technical skill) and that can be applied industrially.

(iii) An invention is not new if at the time of filing a patent application the invention has been published:
  (a) in written form in Indonesia or abroad; or
  (b) verbally or by demonstration in Indonesia.

(iv) Inventions involving a product or a production process are patentable in Indonesia, except for the following:
  (a) inventions contrary to public order, morality or existing law;
  (b) food and drink, including raw material products produced by chemical processes and used to produce food and drink for human and animal consumption;
  (c) new plant varieties or animal species or any process used to breed plants or animals;
  (d) methods of examination, nursing, medication, and surgery applied to human beings and animals (excluding products);
  (e) theory or methodology in the field of science or mathematics.

(v) There is one further exception. The President of Indonesia, by decree, may postpone the grant of a patent for any product or process for up to five years in the public interest, or to support the implementation of development programs in specific areas. This exception does not apply, however, to existing patent holders or pending applications in Indonesia accompanied by priority rights.

2. *Duration of Patent*

Patent protection is for fourteen years from the date established by the Patent Office as the date of receipt of the patent application (which will generally be when the application meets all filing requirements). The commencement and expiration date of a patent will be recorded in the General Patent Register and published in the official Patent Gazette. An extension of two years may be granted on request of the patent holder.

3. *Rights and Obligations of Patent Holder*

A patent holder is granted a special right to use the patent commercially, either personally or by authorization granted to other persons, in one or more of the following ways: (i) to produce, sell, rent, deliver, use, and supply patented products for sale, lease, or delivery; and (ii) to use the patented production process to produce goods and undertake the foregoing activities. A patent holder is obliged to exploit or work the patent in the territory of the Republic of Indonesia.

4. *The Import Exception*

One of the more controversial sections of the new Patent Law, article 20, states that imports of patented products or products made by a patented production process are not deemed to be exploitation/working in Indonesia. Moreover, article 21 states that the importation of patented products or products made by a patented or equivalent production process that were made by someone other than the patent holder will not constitute a violation of the patent in question, except in certain cases which will be specified subsequently in government regulations. It is expected that this particular loophole will be at least partially closed by the implementing regulations as a way of addressing the obvious problems raised by the above articles.

5. *Patent Applications*

Filing fees will be set by regulations at a later date. Patent applications filed by inventors not resident in Indonesia must be filed by a patent consultant registered as such at the Patent Office as proxy of the inventor. The inventor or proxy must declare legal domicile in Indonesia for the purpose of the patent application. The applications must be filed in the local language of Indonesia, namely Bahasa Indonesia.

6. *Civil Action for Infringement*

The patent owner or licensee has the right to file suit for compensation for infringement of the patent. However, the owner or licensee must prove that the infringing product used the patent invention. The judge may order the patent infringer/defendant to cease infringing the patent while the district court investigates the claim.

A patent owner or licensee may also file a claim for delivery up of infringing products or the equivalent value of such products. In such a case the judge has the discretion to order delivery up only after the court has issued a final decision and after the claimant has paid compensation to the defendant where the defendant had acted in good faith. An appeal against a district court decision can be made to the high court and thereafter to the supreme court.

7. *Criminal Action*

Anyone who intentionally and without right violates the rights of a patent holder is subject to seven years' imprisonment and a fine not exceeding Rp 100,000,000 [approximately U.S. $55,000]. In addition to the police, appointed officials of the Department of Justice will be given special investigative authority to conduct patent infringement investigations.

8. *Conclusion*

The new Patent Law will take effect on August 1, 1991. The all-important implementing regulations should be issued just prior to the effective date. For foreign patent owners, the new Patent Law is welcome. In the meantime it would be advisable to review any previous patent application registrations in Indonesia to see which have been made since August 1, 1981. These can be re-registered and, if the old 1953 Decree under which these applications were recorded still has any meaning, they should have priority in 1991.

IV. Malaysia

A. Malaysia to Join Berne Convention

Malaysia announced on January 17, 1990, that it will join the International Union for the Protection of Literary and Artistic Works (the Berne Convention). At present foreign works only qualify for protection under the Copyright Act 1987 if they are published in Malaysia within thirty days of first publication elsewhere, and such publication must be sufficient to "satisfy the reasonable requirements of the public."

The Malaysian Copyright Act, although closely modelled on the copyright statues of other Commonwealth countries, will be amended to satisfy the provisions of the Berne Convention. It is expected that such amendments will be introduced in June 1990, and Malaysia will then accede to the Convention after the amendments become law. One major amendment is the removal of the statutory license granted by the government to itself and its agents to use, reproduce, and adapt works, subject only to payment of "adequate compensation."

Malaysia's joining of the Berne Convention will mean that the proposed bilateral agreements on copyright with the United States and the United Kingdom need not be pursued.

Local reaction to the announcement has generally been positive, with most commentators agreeing that Malaysia needs to provide adequate protection for foreign works as well as receive protection for the works of its own creators. Concern has, however, been raised about the ability of copyright owners to enforce their rights adequately. There has been no indication whether or not the Enforcement Division of the Ministry of Trade and Industry, which presently is responsible for the enforcement of the criminal provisions of the Malaysian Trade Marks Act, will have any role in the enforcement of the Copyright Act.

Foreign copyright owners will also be concerned to see whether or not Malaysia follows the matter through. Although Malaysia joined the Paris Convention (which deals with trademarks and patents) in January 1989, the implementing regulations to put the Convention into effect (for example, handling of "priority" applications) have not yet been issued.

Malaysia has been placed on the United States "watch list" owing to widespread piracy. Washington has hailed the recent announcement, but is noncommittal as to the removal of Malaysia from the "watch list" and will undoubtedly watch the developments closely so as to decide whether Malaysia should be removed from such a list.

V. Philippines

A. The "Control Test" and Corporate Nationality

Certain laws and provisions of the Philippine Constitution limit the ownership of private lands, the exploitation of natural resources, the operation of public utilities, and other nationalized investments to Filipinos or corporations in which at least 60 percent of the equity is Filipino owned. The 60 percent equity requirement is easily determined if the corporation is owned by individual shareholders. The position is complicated if the shareholders are also corporations that, in turn, are owned or partly owned by foreign shareholders.

In the past the Securities and Exchange Commission (SEC) traced ownership of the various corporate shareholders to determine the extent of foreign ownership in a corporation. However, in an opinion dated November 6, 1989, the SEC ruled that the method for ascertaining corporate nationality is to be determined by the "control test." In effect, corporate nationality is now determined by the actual Filipino and foreign equity ownership of the corporation without the need to examine the capital structure of any corporate shareholder in that corporation.

In a recent ruling the SEC held that a corporation that was 70 percent owned by San Miguel Corporation (a 70 percent Filipino and 30 percent foreign corporation) and 30 percent owned by a foreign entity, was qualified to acquire private lands in the Philippines, an acquisition normally restricted to corporations at least 60 percent of the equity of which is Filipino owned. Under the previous rule the corporation would have been refused permission, as its effective foreign equity ownership, taking into account the fact that the San Miguel Corporation was 30 percent foreign owned, would have exceeded the ceiling imposed under the Philippine Constitution. Thus, foreign entities are now able, directly and indirectly, to hold shares in Philippine corporations engaged in nationalized activities to a much greater extent than they could previously.

The "control test" is satisfied only if the Filipino equity ownership in the corporation is at least 60 percent. If the percentage of Filipino ownership in the corporation is less than 60 percent, only the number of shares corresponding to that percentage will be counted as being of Filipino nationality.

VI. Singapore

A. Separation of Singapore and Kuala Lumpur Stock Exchanges

On October 27, 1989, the Malaysian Finance Minister announced that the Malaysian Government wanted Malaysian shares to be delisted from the Stock Exchange of Singapore (the SES). This effectively meant a split between the Kuala Lumpur Stock Exchange (KLSE) and the SES, thus ending a sixteen year-link. The KLSE set December 31, 1989, as the deadline for Malaysian-based companies to delist. To facilitate the delistings, the KLSE amended its listing requirements by removing the need for approval by shareholders at a general meeting before a company can cancel its listing in any recognized stock exchange.

The move is likely to adversely affect the SES, at least in the short-term. Malaysian-based companies account for 182 of the 329 stocks listed on the SES and about 37 percent of the KLSE's total market capitalization. Furthermore, half of all trades in Malaysian shares are executed in Singapore. By contrast, only 54 of the 301 stocks listed on the KLSE are stocks in companies incorporated in Singapore and account for less than 10 percent of SES's market capitalization. The split has prompted a number of responses by the SES and regulatory authorities in Singapore, including: (i) creating an OTC (over-the-counter) market for regional stocks, even if the stocks are not listed in Singapore; and (ii) extending trading hours.

The Monetary Authority of Singapore has called for more new listings to add depth to the local stock market. It is also expected that the market for stock derivatives (such as options, bonds, and warrants) in Singapore will expand. The government is expected to advance its privatization schedules with a view to boost more new listings. In this regard, in an apparently unrelated development, the Singapore Government announced on November 10, 1989, that it will privatize Singapore Telecom by listing it on the SES in approximately three to four years.

VII. South Korea

A. Liberalization of Foreign Investment in South Korea

During 1989 the South Korean Government issued a series of regulations to liberalize its foreign investment approval system. These liberalization measures are the result of the South Korean Government's effort, by opening its market, to avoid the designation as a priority foreign country with trade barriers under the "Super 301" section of the U.S. Omnibus Trade and Competitiveness Act. Summarized below are Korea's recent investment liberalization measures.

(1) Effective July 1, 1989, the South Korean Government no longer imposes so-called "performance requirements" on foreign investors as a condition of approving foreign investment. In the past the government often has made its approval of foreign investment contingent upon performance requirements if, in its view, the investment would substantially affect the domestic industry. These performance requirements include requirements that foreign investors export goods or services, use local materials, achieve a certain level of local equity participation, transfer or license technology, manufacture in South Korea, and the like.

With the abolition of performance requirements, foreign investors, for example, no longer will be required, as a condition of approval, to export goods or services or shift production, distribution, or marketing facilities or techniques to South Korean nationals through government-imposed measures. Even investments with 100 percent foreign equity ownership will normally obtain government approval. In addition, beginning October 1, 1989, foreign investors no longer need to submit a technology transfer plan as part of the application for a tax exemption available to certain categories of high technology industry.

The abolition of performance requirements also applies to previously imposed performance requirements. Existing foreign-invested companies in South Korea, therefore, will not be placed in a disadvantageous position.

(2) From January 1, 1990, all foreign investments in manufacturing with less than 50 percent foreign equity ratio and no tax benefits sought will be subject to "automatic approval," which is a simplified approval procedure involving approximately ten days' review by the Bank of Korea, rather than full review by the Ministry of Finance. (The Ministry of Finance's review lasts thirty days or sixty days depending on the amount of investment.) The ceiling on such investments eligible for automatic approval has been changed from $3 million to $100 million.

From January 1, 1991, the South Korean Government will change the approval system for investments in manufacturing with less than 50 percent foreign equity ratio and no tax benefits into a simple notification procedure.

(3) Effective September 29, 1989, the restriction on the number of directors that a foreign partner can nominate has been repealed. Previously, a foreign investor was not allowed either (i) to nominate more directors than his shareholding ratio entitled him to; or (ii) to have his nominee exercise a casting vote where domestic and foreign investment are equal. Depending on the agreement between the joint venture parties, a foreign investor with less than 50 percent equity can now exercise management control.

(4) The amended Guidelines for Foreign Investment Approval opened the following sectors to foreign investment: (i) pharmaceutical wholesaling; (ii) sea

freight forwarding and sea freight brokerage (less than 50 percent equity); (iii) insurance brokers and agents (exclusive agents only); and (iv) pharmaceutical manufacturing. The government has also confirmed its commitment to open the following industrial sectors: (i) travel agencies (100 percent equity from 1991); (ii) advertising agencies (up to 100 percent equity from 1990, 100 percent equity from 1991); (iii) cosmetics wholesaling (100 percent equity from July 1990).

(5) Restrictions on foreign investment in some manufacturing sectors have been removed to ensure 100 percent foreign investment. Previously, investment in these sectors was approved only by way of a joint venture with existing domestic manufacturers. Such manufacturing sectors include: (i) motor vehicles; (ii) diesel engines (320 horsepower or above); (iii) silicon steel, manganese steel, and silicon-manganese alloy steel; (iv) excavators, loaders, bulldozers, cranes, and motorgraders; (v) optical fibers, optical fiber-covered wires, and cables; (vi) electronic switching systems; and (vii) transformers, circuit breakers, gas-insulated substations, and disconnecting switches for ultra high voltage use.

(6) The South Korean Government, in a move parallel to the abolition of performance requirements for equity investment, will establish a plan to remove the authority of the relevant ministry in requesting changes to provisions contained in a technology licensing agreement. Under the new plan a licensing agreement will be screened only under the Antitrust and Fair Trade Law.

VIII. Taiwan

A. Proposed Tax Law Amendments

The Executive Yuan of the Republic of China Government has announced three tax amendment proposals:

1. *Income Tax*

The 1990 income tax amendment proposal, which makes some major changes in the Income Tax Law, provides for, inter alia: (i) elimination of income tax on stock transfer transactions; (ii) extension of the loss carry forward period from three years to five years; (iii) reduction of personal income tax rates from the current maximum of 50 percent to 40 percent; and (iv) simplification of tax brackets from the current thirteen levels to five levels.

2. *Securities Transactions Tax*

The securities transactions tax rate on stock transfers is to be increased from the current 0.15 percent to 0.6 percent, following the proposed elimination of income tax on stock transfer transactions. It is also proposed that the securities transactions tax rate on transfers of corporate bonds and other government-